REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF UMHLABUYALINGANA MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Umhlabuyalingana Municipality which comprise the statement of financial position as at 30 June 2009, and the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory notes as set out on pages [xx] to [xx].

The accounting officer's responsibility for the financial statement

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the Standards of Generally Recognised Accounting Practice (Standards of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of

expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

6. Paragraph 11 *et seq*. of the Standards of GRAP, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Umhlabuyalingana Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.

   Consequently, a decision has been taken that the Auditor-General South Africa will not audit the budget information presented in the financial statements in terms of GRAP 1 and the audit opinion will, therefore, not cover such information.

7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

8. In my opinion the financial statements present fairly, in all material respects, the financial position of the Umhlabuyalingana Municipality as at 30 June 2009 and its financial performance and cash flows for the year then ended, in accordance with the Standards of GRAP and in the manner required by the MFMA.

Emphasis of matters

Without qualifying my opinion, I draw attention to the following matters:

Going concern

9. As disclosed in note 25 to the financial statements the Municipality prepared the financial statements on a going concern basis and continues to operate, however, there are a number of indicators that its financial sustainability is under threat. The Municipality had difficulties in paying staff their October 2009 salaries amounting to R1 188 142 with salaries being paid three days after the official pay day.

   At year end the Municipality had unspent conditional grants amounting to R7 634 898 disclosed in their financial statements which were not cash backed / supported by separate investments, and the primary account reflected a cash book overdraft of R933 026. Furthermore, Municipal Infrastructure Grant funding of R7 268 000 had also been withheld.

Suppliers' invoices amounting to R106 403 were not paid within 30 days of receipt thereof, further highlighting the cash flow and going concern problem being experienced by the municipality.

Without MIG funding and considering that the municipality has no rates income, no service delivery would take place to the community as the funding received by the Municipality as part of their equitable share is used for employee remuneration and running expenses. The amount of equitable share received for the year under review was R22 196 390 and grant funding of R11 131 306, totalling R33 327 696. Of this funding 90% was spent on remuneration of staff and councillors and daily operating expenditure of the municipality.

Unauthorised expenditure

10. As disclosed in note 29 to the financial statements, the budgeted expenditure per department was exceeded by five departments (Management, Executive and Council, Corporate Services, Community Services and Technical), however, no Council resolution was provided that the over-expenditure of R1 214 957 was approved by Council.

Fruitless and wasteful expenditure

11. As disclosed in note 28 to the financial statements, fruitless and wasteful expenditure relating to interest amounting to R11 458 was incurred as a result of the late submission of EMP201s and the late pay-over of Pay As You Earn and Standard Income Tax of Employees deductions to the South African Revenue Services.

Irregular expenditure

12. As disclosed in note 27 to the financial statements, irregular expenditure of R7 634 898 was incurred by the municipality as a result of Grant Funding being used for daily operational expenditure, and not in terms of the grant conditions.

    As disclosed in note 27 to the financial statements, payments totalling R36 663 were made to a supplier, of whom a member was an employee of the State. This was contrary to regulation 44 of the municipality's Supply Chain Management (SCM) policy.

Restatement of corresponding figures

13. As disclosed in 21 to the financial statements, the corresponding figures for 30 June 2008 have been restated as a result of a change in accounting policy and errors discovered during 2008/2009 in the financial statements of the municipality at and for the year ended 30 June 2008.

Other matters

Without qualifying my opinion, I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Material inconsistencies in information included in the annual report

14. I have not obtained the other information included in the annual report and have not been able to identify any material inconsistencies with the financial statements.

Unaudited supplementary schedules

15. The municipality provided supplementary information in the Annexure E1 and E2 to the financial statements on whether resources were obtained and used in accordance with the legally adopted budget, in accordance with GRAP 1 *Presentation of Financial Statements.* The supplementary budget information and other supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules, accordingly I do not express an opinion thereon.

Non-compliance with applicable legislation

Municipal Systems Act

16. Not all councillors declared their interest / fully disclosed their interests held by them within 60 days after being elected as required by section 54 of the MSA.

17. Managers appointed in terms of section 57 of the MSA did not fully declare all their interest held by them as required by section 69 (section 5A of schedule 2) of the MSA.

Municipal Finance Management Act

18. Invoices totalling R106 403 were not paid within 30 days of receipt thereof as required by section 65(2)(e) of the MFMA.

19. Reports in respect of the irregular expenditure were not made by the accounting officer to the Mayor, MEC for Local Government and the Auditor-General as required by section 32(4) of the MFMA.

Supply Chain Management Policy

21. Regulation 44 of the municipality's SCM policy in terms of the MFMA was not adhered to as payments totalling R36 663 were made to a supplier, of which one of the members was an employee of the State.

Governance framework

22. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the key governance responsibilities addressed below:

Key governance responsibilities

23. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
Clear trail of supporting documentation that is easily available and provided in a timely manner			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.		☐
Quality of financial statements and related management information			
2.	The financial statements were not subject to any material amendments resulting from the audit.		☐
3.	The draft annual report was submitted for consideration prior to the tabling of the auditor's report.		☐
Timeliness of financial statements and management information			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines per section 126 of the MFMA.	☐	
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.		☐
Development and compliance with risk management, effective internal control and governance practices			
6.	Audit committee		
	• The municipality had an audit committee in operation throughout the financial year.	☐	
	• The audit committee operates in accordance with approved, written terms of reference.	☐	
	• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.		☐
7.	Internal audit		
	• The municipality had an internal audit function in operation throughout the financial year.	☐	
	• The internal audit function operates in terms of an approved internal audit plan.	☐	
	• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.		☐
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		☐
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		☐

No.	Matter	Y	N
10.	The information systems were appropriate to facilitate the preparation of the financial statements.	☐	
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.		☐
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	☐	
Follow-up of audit findings			
13.	The prior year audit findings have been substantially addressed.		☐
14.	SCOPA/Oversight resolutions have been substantially implemented.	☐	
Issues relating to the reporting of performance information			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		☐
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		☐
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the municipality against its mandate, predetermined objectives, outputs, indicators and targets section 68 of the MFMA.	☐	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.	☐	

24. The drivers resulting in the above-mentioned negative responses were as a result of the lack of availability of the Municipal Manager and Chief Financial Officer during the audit, compounded by the inadequate filing system in place at the auditee resulting in documentation being produced way after the agreed upon time-frames.

Investigations

25. An investigation was conducted by an independent firm on request of Department Local Government. The investigation was initiated based on the allegations of possible related party transactions and misappropriation of grant funding / expenditure irregularities. The investigation has not been finalised at date of this report.

26. The municipality engaged a separate firm to investigate the irregularities in respect of purchases / tenders to certain suppliers as had been indicated by Council, however, no report was made available to me in respect of the investigation undertaken.

27. The Council suspended the Municipal Manager and Chief Financial Officer during October 2009 on full pay for a period of two months pending an investigation outcome, as a result of mismanagement of municipal funds. At the date of this report it could not yet be determined whether the Municipal Manager and Chief Financial Officer's services would be terminated or whether they would be re-instated.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

28. I have reviewed the performance information as set out on pages xx to xx.

The accounting officer's responsibility for the performance information

29. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

The Auditor-General's responsibility

30. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
31. In terms of the foregoing my engagement included performing procedures of a review nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
32. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the findings reported below.

Findings on performance information

Non-compliance with regulatory requirements

33. The integrated development plan (IDP) of the municipality did not include a financial plan, as prescribed by section 2(3)(c) of the Municipal Planning and Performance Management Regulations (MPaPMR).
34. The key performance indicators set by the municipality did not include all the general key performance indicators applicable to the municipality, as prescribed by section 43(2) of the MSA.
35. The development priorities set out by the municipality did not include all the outcome indicators, as prescribed by regulation 9(1)(a) of the MPaPMR.
36. The performance targets set out by the municipality in the IDP were for a period of one year and not five years, as prescribed by regulation 6 of the MPaPMR.
37. The Service Delivery and Budget Implementation Plan (SDBIP) of the municipality indicates targets set for each quarter, but does not indicate performance indicators for each quarter, as prescribed by section 53(3) of the MSA.
38. The SDBIP was not approved by the Mayor within 28 days after the approval of the annual budget, as prescribed by section 53(1)(c)(ii) of the MFMA.

39. The performance of the service provider is not included in the annual performance report, as prescribed by section 48(1)(a) of the MSA.

40. The IDP of the municipality contained development objectives that were not included in the SDBIP, and performance indicators and performance targets per the IDP were not the same as the performance indicators and performance targets per the SDBIP, as prescribed by section 53(c)(iii)(bb) of the MSA.

41. The annual performance information report of the municipality did not contain measures taken or to be taken to improve on performance, as prescribed by section 46(1)(a)(iii) of the MSA.

42. The annual performance information report of the municipality does not clearly indicate what targets were achieved and which were partially achieved, and what work was done in achieving the targets, as prescribed by section 46(1) of the MSA.

43. The annual performance information report of the municipality does not indicate reasons for over-exceeding of certain targets, and some of the performance indicators in the annual performance report did not contain targets, as prescribed by section 46(1) of the MSA.

44. The annual performance information report of the municipality did not contain comparisons for some of the performance indicators between the 2007-08 and 2008-09 financial year, as prescribed by section 46(1) of the MSA.

45. The annual performance information report of the municipality does not include measures to be taken to improve performance, as prescribed by section 46(1) of MSA.

46. The annual performance report included the organisational scorecard as well as the individual scorecards of the section 57 managers, thereby duplicating development objectives which is not in accordance with section 46(1) of the MSA.

Usefulness and reliability of reported performance information

47. The following criteria were used to assess the usefulness and reliability of the information on the municipality's performance with respect to the objectives in its IDP and SDBIP:

    - Consistency: Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved IDP and SDBIP?
    - Relevance: Is the performance information as reflected in the indicators and targets clearly linked to the predetermined objectives and mandate. Is this specific and measurable, and is the time period or deadline for delivery specified?
    - Reliability: Can the reported performance information be traced back to the source data or documentation and is the reported performance information accurate and complete in relation to the source data or documentation?

The following audit findings relate to the above criteria:

Inconsistently reported performance information

48. The IDP of the municipality contained development priorities, objectives and key performance indicators that were inconsistent with those that were reflected in the SDBIP and the annual performance information report.

Reported performance information not relevant

49. The targets contained in the annual performance information report of the municipality were not:

    - Specific in clearly identifying the nature and the required level of performance,
    - Measurable in identifying the required performance.

Reported performance information not reliable

50. The measures and targets reported on in the annual performance information report of the municipality were either not supported by appropriate audit evidence provided or the evidence provided to support the reported information did not adequately support the accuracy and completeness of the facts reflected in the report.

APPRECIATION

51. The assistance rendered by the staff of the Umhlabuyalingana Municipality during the audit is sincerely appreciated.

Auditor-General

Pietermaritzburg

28 January 2010

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence